



TITLE:

THE LINK SYSTEM IN JAPAN

AUTHOR(S):

Taniguchi, Kichihiko

CITATION:

Taniguchi, Kichihiko. THE LINK SYSTEM IN JAPAN. Kyoto University Economic Review 1939, 14(2): 33-54

ISSUE DATE:

1939-04

URL:

https://doi.org/10.11179/ker1926.14.2_33

RIGHT:

Kyoto University Economic Review

MEMOIRS OF
THE DEPARTMENT OF ECONOMICS
IN
THE IMPERIAL UNIVERSITY OF KYOTO

VOLUME XIV
1939

PUBLISHED BY THE DEPARTMENT
OF ECONOMICS IN
THE IMPERIAL UNIVERSITY OF KYOTO

THE LINK SYSTEM IN JAPAN

By KICHIHIKO TANIGUCHI

CONTENTS

1. The Link Trade and the Clearing Trade
2. The Characteristics of the Link System
3. The Link System as an Export Promotion Measure
4. The Functions of the Link System
5. Various Types of the Link System

1. THE LINK TRADE AND THE CLEARING TRADE

The link system is a new device of international trade now widely discussed and partly realised in Japan. We have been advocating from time to time the adoption of such a system in our country,¹⁾ and it is a cause for congratulation, from the point of view of our wartime international trade, that this system has at last been adopted; even though we feel that this step should have been taken much earlier. It is, we believe, a system of such vast significance that it must inevitably serve to mark an epoch in the history of our foreign trade policies. Availing ourselves of this opportunity, we propose to discuss a few problems pertaining to the newly instituted system.

What are the essential characteristics of the link system? What are the principal points at which the new system differs from similar trade devices adopted in the past or by foreign countries? These questions seemingly deal with abstract theories, but without a clear grasp of

1) Cf. my book, *The Foreign Trade Policy of Japan*, 1937, Chapt. IV, Various Problems of Wartime Trade Control, p. 489 ff. Also my essays: *Measures for Wartime Trade Promotion*, the Economist, January 1, 1938; *New Export Promotion Measures*, the Osaka Asahi, March 14, 1938; *Problems of Foreign Trade under Prolonged War Conditions*, the Central Review, May, 1938. (In Japanese.)

these fundamental questions, it is hardly possible to provide adequate solutions to the various problems that arise in the operation of the system. In some of the studies previously published,²⁾ we have divided the various foreign trade methods into two classes, namely, (1) the exchange trade systems, which comprise those foreign trade transactions which are settled by means of exchange, and (2) the clearing trade systems, which include those controlled not by exchange but by the clearing systems. The link system under discussion is not a method of counterbalancing imports with exports. On the contrary, it is a system whereby each item of import or export is controlled by exchange with some other item. According to the foregoing classification, the link system is not a clearing system but rather a new trade method falling into the category of an exchange system.

In this respect the link system is the antithesis of the clearing system. It differs also from the *Waren-clearing-system* or the *Kompensationsgeschäft* now widely adopted in Germany, for these latter methods are characterized by their independence of exchange settlement.³⁾ In so far as the term "link system" is used in the broad sense so to include all manner of foreign trade transactions that establish a link between imports and exports in one form or another, the *Kompensationsgeschäft* adopted in Germany may be considered as a form of the link system. In the present study, however, the term "link system" is used in its narrower sense, and is to be distinguished from the *Kompensationsgeschäft* solely by the fact that it relies upon exchange settlement, while the latter does not. In other words, while the link system merely stipulates that the import permit is granted in conjunction with certain specific exports,

2) Cf. my essays; *The Theories of the Clearing Trade System*, the Kyoto Imperial University Economic Review, June, 1938; *Various Forms of the Clearing Trade System*, July, 1938. (In Japanese.)

3) Cf. the abovementioned essays in the Kyoto Imperial University Economic Review, June and July 1938.

the *Kompensationsgeschäft* requires not only a linking between imports and exports but the counterbalancing imports with exports as well, thus entirely dispensing with exchange settlement. This constitutes the most fundamental difference between the two systems.

The link system is a foreign trade method unique in Japan, its closest counterpart being the *Kompensationsgeschäft*, from which our Japanese system has adopted more essential features than from any other. It was the difference in the circumstances by which the two countries were faced, that the *Kompensationsgeschäft* developed in Germany and the link system in Japan. What then were these circumstances? Subsequent to the financial crisis in July, 1931, Germany imposed restrictions upon the import trade by a stringent control of foreign exchange, until June, 1934 in fact, when she was compelled to declare a transfer moratorium and suspend repayment of all external debts. Almost every new foreign trade measure thereafter adopted in Germany has been a device built upon this principle of suspending the discharge of foreign obligations. Consequently, all the new foreign trade systems subsequently adopted have invariably embodied the principle which forms the basis of the clearing system, namely, importation without external payment. The formal agreement between states that legalizes this principle constitutes the so-called exchange clearing system, while the private agreements between individuals emerge as exchange clearing transactions of various types.

The situation that has prevailed in this country in recent years resembles in many respects the condition in Germany, but Japan has neither declared a transfer moratorium nor does she contemplate doing so. On the contrary, the non-payment of external obligations is simply not practical, inasmuch as the assurance of the continued importation of war supplies has come to constitute the cardinal problem of Japan's economic affairs, since the reorganization of her national economy upon a wartime basis two years

ago. It is a well known fact that with a view to insuring the importation of war supplies, the imports to meet popular demands have been placed in Japan under rigorous control, by means of the import permit system or the import exchange permit system. It is true that the import permit system has been designed to restrict external payment, and that it is similar to the German system in this respect. Nevertheless, there are some differences between the direct suspension of external payment and the restrictions of imports by a permit system. This latter system constitutes the basic measure of our import control, the import permit being issued on the basis of linking imports with exports. In other words, the import of goods is permitted on the basis of an export transaction already completed, or on the condition that it will be completed as a future obligation. This, in fact, is the basic element of the link system as defined in the narrower sense.

Thus the link system differs from the clearing system in its nature as well as in its origin. As a natural consequence, it differs from the latter also in the process through which it is brought into existence. The outstanding difference in this respect is found in the fact that while the clearing system comes into existence in consequence of a bilateral agreement between the states concerned, the link system is enforced by the unilateral action of one state. As a matter of fact, the link system in Japan has been put into operation, not by agreement with foreign countries or foreign merchants, but merely by the government's announcement of the enforcement of the regulation to foreign trade merchants within the country. The German system of clearing trade, on the other hand, becomes effective only by mutual agreement between two states or two individuals, which stipulates that the trade balances of the interested parties shall be offset by mutual sales or purchases. This is process of organizing a clearing system implicit in the nature of the system itself. Here again we note an essential

characteristic of the link system that distinguishes it from the clearing system just described.

2. THE CHARACTERISTICS OF THE LINK SYSTEM

Link trade is a form of exchange trade, inasmuch as it appears to liquidate the trade balance by means of exchange. What then is its relation to various other types of the exchange trade, particularly to those developed in recent years; and wherein does it differ from them? It goes without saying that the system of link trade is one of the new methods of trade control, for it imposes a direct control upon the volume of international trade. The question that remains to be answered is its relation to other types of controlled trade.

1. The quota system. There is an obvious difference between the quota system and the link system. The former system seeks to control the import trade as such, without reference to the export trade, by dividing specified imports externally among various exporting countries, or domestically among the importers within the country. However, the quota system has certain characteristics in common with the link system, in that it is a species of import restriction frequently employed for the promotion of the export trade by linking exports with imports. In case, for example, the import quotas for various exporting countries are determined not in conformity with the past trade volume, but in direct proportion to the exports to each country, then the system is operated along the line of link system. In case the import quotas are imposed upon foreign countries or individuals as a means of intensifying the restrictions on imports, the system becomes a means of import control. When it is adopted as a means of insuring export in return for the import of a specified quota, it becomes a method of export promotion. In all of these cases, however, the quota system differs from the link system, by reason of the fact that the former takes place between two states

and because the maximum import quotas are determined from the beginning. In the link system, on the contrary, the import volume is not determined but is variable in proportion to the exports. In view of this particular difference, the quota system might be called an absolute quota system and the latter a relative quota system.

2. The barter system. The barter system also comprises a number of types, which, with the exception of those designed to offset imports directly by exports, generally contrives to link certain specific imports with specific exports, such as the exchange of raw cotton for cotton piece-goods, as stipulated by the Indo-Japanese Trade Agreement. Barter systems of this nature, therefore, can be regarded as types of the link system, even though there are certain differences between the two groups. One of these differences is found in the fact that while the link system operates with individual merchants or trading organizations as units, the barter system establishes a link between the total specific imports of a state and its total specific exports; the system itself being enforced mutually in the states concerned in consequence of a bilateral agreement. Another difference lies in the fact that the barter system is usually resorted to as a means of overcoming difficulties in the promotion of the export trade, or in preventing a recession, while the latter system is designed to moderate the import restrictions already in force by means of linking between imports and exports. No doubt the link system may also serve to promote the export trade, and in fact it was invoked in this country primarily for that very purpose. But, as will be discussed later, the extent to which this result can be achieved is proportional to the degree to which a moderation of the import restrictions is desired, the success achieved in this respect being practically negligible where the demand for moderating the import control is not strong. At any rate, the promotion of the export trade, if realised at all, is an indirect result of the link system, although it constitutes the primary end

of the barter system which determines the export volume by agreement.

3. The import licence system. The licence system resembles the link system more closely than any other trade device in that it also presupposes the restriction of imports. An obvious difference between the two is the basis on which the issue of the import licence is regulated. In the licence system, the past business turnover provides the principal basis of consideration, the licence being granted to the importer allowing him to import up to a certain percentage of his past business volume. In the link system, on the contrary, the licence is granted in accordance with the export business accomplished, irrespective of the past business turnover. In a certain sense, therefore, the latter represents a variant of the licence system.

Thus considered, the link system appears as a new trade device falling under the exchange trade system and distinct from the quota system, the barter system, or the licence system, though closely related to each of them. For the time, let us define it as a system which permits individuals or organizations to import in quantitative link with certain specified exports. Hence it is preceded by import restrictions or licence systems.

In establishing an linking between exports and imports for individual traders or organizations, imports can be linked with exports or exports with imports. Accordingly as one or other of these two processes of linking is adopted, the link system may be divided into an import privilege system and an obligatory export system. The former is a system for permitting imports in link with export trade already completed, which thus gives the exporter the privilege to import. The latter, on the contrary, is a system of obligatory export, since the import trade already permitted is to be linked with the export trade to be completed as a necessary condition. This system of obligatory export is sometime taken broadly as synonymous with the link system itself, which really comprises both of these linking

processes. But, strictly speaking, there should be a clear distinction between the two.

The question may now be raised as to which of these methods of linking is preferable. In view of the circumstances now prevailing in this country, which made it imperative to adopt the trade device under discussion, it is apparent that preference should be given to the system of import privilege, in other words to the system of permitting imports in link with export trade already concluded. The reason is obvious. The system of obligatory export, in other words import permits granted on the basis of export shipment to be made in future, entails uncertainty due to the possible failure of that export trade to materialize, and to the difficulty of cancelling permits already granted, in case the export trade does actually fail. For the above reason, this system may prove ineffective in either restricting imports or promoting the export trade. On the other hand, the practice of granting import permits in return for the export business concluded eliminates this uncertainty and encourages the export trade by prompting traders to export in order to acquire the privilege of importing in the future. Thus this method of linking will, it is anticipated, prove more effective both for the restriction of imports and for the promotion of the export trade.

The privilege to imports enjoyed under the link system is apt to be at a premium, since the person who has acquired it by reason of having completed an export transaction can transfer his privilege to another person who wishes to import. Under the system of obligatory export, on the contrary, the transfer of import privileges apparently does not take place. In reality, however, those who fail to fulfil this obligation may seek the transfer of export quotas from others who have exported without such obligation or in excess of the required volume. Therefore, in so far as the practice of transferring import privilege is permitted, the question of premium will arise unavoidably even under the system of obligatory export. Should the transfer be

prohibited, the premium would not appear even under the system of import privilege. Moreover, while the problem of premium is generally regarded as an evil arising only under the individual link system, it may possibly arise under the group link system as well. For example, an export association which has shipped extensive exports might transfer its import privileges to another association. Where the transfer of import privilege is permitted, there is no way of prohibiting the transfer being made at a premium. This abusive practices can be eliminated only by prohibiting the transfer of the import privilege itself.

3. THE LINK SYSTEM AS AN EXPORT PROMOTION MEASURE

It is primarily as a means of promoting the export trade that the link system has come to attract public attention in this country. Will it really prove effective in fostering export activities as was expected? Among the various functions of the link system, let us study first of all this particular aspect of the subject.

The link system is undoubtedly a more effective measure than a mere licence system for the promotion of the export trade, and it is for this reason that we have advocated its adoption. In ordinary import restriction or the licence system, the import trade is considered by itself without reference to the export trade, with the result that the attendant rise in the price of imported raw materials tends to decrease the volume of exports manufactured therefrom, thereby compelling the imposition of more stringent control upon imports. Thus import restriction when imposed upon the import trade alone is likely to result in an increasingly rigorous control of imports.

The imports now placed under restriction comprise not only non-essential and non-emergency supplies, but indispensable raw materials as well. It is solely for the purpose of maintaining our international trade results in balance

that the importation of these important raw materials is limited, in spite of keen demands for them. Whenever an improvement results in our foreign trade balance, say, from an increase in exports, the further importation of these materials is permitted. This, in fact, is the theoretical basis of the link system. Whether or not the system will successfully increase our exports depends mainly upon the intensity of the demand for imports. Where the need of certain imports is imperative or the profit resulting from their importation is lucrative, every effort will be made to export in order to acquire the privilege of importing these materials. If, on the other hand, the demand for imports is not intense or if the profits are negligible, the desire for the import privilege becomes proportionately weak, and the system contributes but little to the promotion of the export trade. In the cotton link system, imported raw cotton is used mainly as materials for exports, and hence the demand for imported raw cotton is proportional to the export of cotton piece-goods. In so far as the cotton link system is concerned, therefore, export promotion does not result from the system itself but from certain other factors. The main problem is as to whether the system is effective in lowering export price.

One of the causes that tend to lower export prices in link trade is premium. So long as the import privilege acquired in return for export trade completed is transferable at a premium, export price can be lowered in the amount of the premium earned, thereby giving rise to a kind of export dumping. Such premium payment on import privilege, however, enhances the price of imported materials, which in turn tends to offset the reduction of export price effected by the premium earned, to the detriment of the export trade. In case a portion of the imported materials is diverted to war supplies or domestic consumption, as in the case of the wool link, etc., the premium earned can be applied to cover a part of the cost, although even this is not easily achieved when domestic prices are placed under

intensified government control. It is still more difficult in the case of the cotton trade, wherein the entire quantity of imported materials is destined for exportation.

Does it follow, then, that high cost of imported raw materials, resulting from premium payment, constitutes an obstacle to the promotion of the export trade? The line of argument with regard to this problem appears to run parallel with the theory of exchange dumping. Theoretically, exchange dumping is impossible, since the cost of imported materials rises in proportion to the decline in exchange. In reality, however, exchange dumping has been practiced in Japan over a relatively long period. As discussed at other place,¹⁾ exchange dumping is impossible, both theoretically and practically, where imported materials are re-exported in their original condition. As a matter of fact, however, a large portion of our imports, particularly in the case of imported raw materials, is re-exported as manufactured or semi-manufactured goods. In other words, imported materials are fabricated together with domestically supplied materials and by domestically supplied labour. It is these domestically supplied factors that are subject to exchange dumping. Thus along with the progressive increase in domestic factors from pure re-exports to pure domestic products, exchange dumping becomes progressively significant.

Let us now observe whether this theory is applicable to the problems of link trade premium. A superficial observation seems to show that link trade premium does not favorably affect the trade in the case of pure re-exports, since the reduction in export prices is offset by the rise in import prices; and that the export trade in pure domestic products alone enjoys any benefit, since the premium does not affect the cost of these products. A more careful analysis, however, would reveal that the declining exchange rates and link trade premiums affect the export trade in

1) Cf. my book, *Foreign Exchange*, 1937, p. 121. (in Japanese)

entirely different ways. In the last analysis, these differences are reduced to the fact that while exchange rate affects the trade *pro rata*, link premium influences it in terms of an absolute amount of money. The amount paid by an importer as a premium for the acquisition of the privilege to import limits the extent to which export goods are dumped abroad and to which import prices may be advanced. Hence, in an hypothetical case in which the linked exports and imports were of an equal amount and the premium paid for the acquisition of import privilege was 10%, the export price would be reduced by 10% and the import price raised by the same percentage. In actual transactions, however, it seldom happens that exports of a certain amount are linked with imports of an equal amount. In most cases the export exceeds the import. This is equally true in case imports are re-exported after domestic fabrication. Under such circumstances, the export dumping effected with the premium earned is of a relatively small proportions as compared with the rise in import prices. In other words, a certain amount of premium being borne by a relatively small volume of imports, the resultant advance in import prices is proportionally greater than the extent of export dumping.

On the other hand, the growth of the export trade depends not upon the amount of export dumping, but upon the ratio at which export price is to be lowered. In so far as this ratio is smaller than that of the advance in import price, as just noted, the link system cannot be expected to play an important rôle in export trade promotion without the aid of other factors. In the actual process of trade operation, however, it may sometime happen, at least as a temporary phenomenon, that the export trade is given a strong impetus in consequence of a large incidence of export dumping and a large reduction in export prices resulting from the earning of an excessively large premium. But such an impetus lasts only so long as the stock of raw materials is available, and since new supplies of imported

materials are usually available only at much advanced prices, encouragement for export trade from this source ceases to be felt, unless it is sustained by other factors. The appearance of such a temporary impetus as above mentioned is due to the rise in the amount of link trade premium, due to an intense demand for imports or to the unusually large profits that can be earned from the importation of such materials. When this premium is restricted or entirely prohibited, the export trade will practically cease to receive any encouragement for its expansion through this particular channel.

What is the other factor referred to above that tends to promote the export trade? As in the case of exchange dumping, it consists of the domestic factors added to exports, such as domestically supplied raw materials and labour. By lowering the cost of these factors, any higher rise in the price of imports can be offset by a corresponding reduction in export price. In a certain sense of the word, this constitutes a dumping of labour and national resources. However, whether or not this actually represents dumping can be determined only by comparing the price of domestic raw materials with their production cost on the one hand and wages with the level of domestic commodity prices on the other.

Wherever such a reduction in the cost of domestic factors of production is possible, the link system can bring about an increase in the export trade even in the absence of dumping resulting from link trade premium. And the prohibition of premium does not necessarily deprive the link system of its capacity to promote the export trade. Where importation of foreign materials is necessary or profitable, traders or trading organizations will endeavor to increase exports. And to attain this object, export prices must be lowered at the expense of domestic factors of production, regardless of whether or not the price of imported raw materials is actually enhanced. The sweeping changes made, for better or worse, in the control system of the

cotton industry, in preparation for the institution of the cotton link system, become significant, when they are considered in the light of the foregoing argument. It is considered necessary for the promotion of the export trade to eliminate the friction that existed in the industry and to establish the dominance of large-scale establishments as a means of enforcing a reduction in the cost of the domestically supplied factors of production.

The capacity of the link system to promote the export trade, regardless of whether or not it accompanies the problem of premium, is dependent upon the extent to which export prices can be curtailed at a lowered cost of the domestic factors of production. Of the various domestic factors responsible for the production of export goods, those which are most susceptible to reduction in this country today are wages and profit. It is for this reason that the piece-work system has been generally adopted in the cotton piece-goods industry. Should large-scale cotton mills undergo as great a sacrifice proportionally as is borne by petty weavers and their employees, much progress could be achieved in the exportation of cotton piece-goods. Under the present system, which fails to make a satisfactory provision in this respect, large-scale mills enjoy advantages to the detriment of their petty competitors, and hence it would be absurd to anticipate any substantial improvement in the export trade. Furthermore, under the existing conditions of wartime economy, there are certain obstacles which stand in the way of reducing the cost of the domestic factors of production. In the first place, under present wartime conditions, as contrasted with periods of depression, there is a scarcity of material and of labour supply, which prevents any undue reduction in the cost of these production factors. In the second place, where prosperous war industries co-exist with less active industries, the psychological effect of cost reduction must be taken into account, even if it were possible to reduce the cost of these factors adequately. This again prevents the reduction

of cost below a certain minimum level.

The present inactivity of our export trade is attributed principally to (1) the economic depression in America and other countries, (2) the boycott of Japanese goods arising out of the China Incident, and (3) the rise in commodity prices within the country itself. Leaving the problem of boycott aside, for the time, the other two causes of trade recession can be overcome only by reduction in export prices. The merit of the link system in this respect is dependent, as aforementioned, upon the possibility of lowering the cost of the domestic factors of production and upon the sacrifices that can be imposed upon large-scale capitalistic enterprises. Since there is a limit to the first method and no certainty as to the second possibility, the link system should not be expected to prove very effective as an export promotion measure. Unless this system is enforced in conjunction with more drastic measures of control, it would seem impossible to reach the desire goal.

4. THE FUNCTIONS OF THE LINK SYSTEM

One of the principal economic functions of the link system is the promotion of the export trade as discussed above, while a second and no less important function is the moderation of import restrictions.

1. The link system is enforced, as aforementioned, on the basis of the restriction of imports in general and of indispensable raw materials in particular. Where there is no restriction or the restriction is imposed merely on non-essential and non-emergency materials, the link system cannot be expected to fulfil its functions properly. When, however, the restriction becomes so stringent as to include essential raw materials, it becomes possible to permit imports in link with exports. Under this system, therefore, import permits are issued under definite restrictions, the importation of non-emergent and non-urgent supplies being prohibited, even though in compensation for export already

completed. Accordingly, import restrictions can be moderated by the link system only within the limits established on the basis of designated classes of merchandise which are regarded as indispensable for the national economy.

2. In the so-called individual merchandise link system, import permits for the importation of certain raw materials are granted only in link with the exports manufactured with these materials. Hence even essential raw materials are excluded, unless they are destined for exportation as manufactured goods. To remedy this shortcoming, a collective merchandise link system has been separately instituted, providing for the issue of import permits covering several classes of merchandise. In this case, however, the import permit parallels a limitation based on merchandise as above discussed.

3. Import values are also subject to restriction. Theoretically, import permits should be issued without any restriction so long as there is a corresponding increase in exports. However, the system is not enforced so as to allow importation up to the full amount of corresponding exports. From this maximum set by the volume of the corresponding exports, the proportional amount of the imports permitted is supposed to vary in accordance with the type of merchandise and the needs of the national economy. It follows, therefore, that the total volume of imports permitted under the link system is smaller than that of the corresponding exports, and the difference between these two amounts represents the value of materials imported independently of the link system.

4. Even where the link system is in force, there are certain classes of merchandise, such as war supplies, which are given preference in importation. These supplies are imported unconditionally, without corresponding export, in order to meet the requirement of wartime activities, thus remaining beyond the control of the link system. The link system, then, is not a substitute for the import licence system or for general import restrictions, but a system

operating only partially within the wider field of restrictive control. Hence there are certain groups of merchandise which are imported without reference to the link system, while there are other items which are prohibited even under this system. It would follow from the foregoing that with the increase in the amount of preferential imports the difference between the volume of total imports and total exports would tend to become greater, and that the trade balance representing the excess of exports would be applied to payments for munitions and other war supplies purchased from abroad.

It has been clearly shown by the foregoing discussion that the import transactions carried on under the control of the link system are subject to many restrictions. Nevertheless, compared with the licence system of the past, the link system represents a much less severe method of controlling imports. Aside from munition and non-essential or non-emergent goods which are unaffected by this system, the raw materials destined for export, which are the principal objects of link trade control, may actually be imported almost limitlessly, though in definite proportions, so long as there are parallel increases in the export of the corresponding manufactures, a fact which may be regarded as fully demonstrating the accuracy of the foregoing conclusion. As a practical problem, however, the margin of moderation in import restriction seems to be very limited, since the system does not appear very effective in promoting export trade.

The third function of the link system which should not escape our attention is that of balancing the export with import trades. Should this system of linking imports with exports be operated so as to cover the entire foreign trade of a state, the relation between imports and exports could be adjusted theoretically in accord with the results desired. In other words, by varying the ratio at which the link is to be established, foreign trade could be adjusted *ad lib* to show either an excess of exports or an excess of imports,

or to remain in balance. However, as a matter of fact, the link system is built upon a more comprehensive system of import licence with allowances for preferential imports, and it would, therefore, seem that the link system is being operated to show an excess of exports, while the wider control system is designed to bring about a foreign trade equilibrium. It is of course possible, theoretically, manipulate the control system so as to secure either an excess of exports or an excess of imports. In practice, however, the link system is ordinarily operated for the purpose of moderating import restrictions imposed for some reason or other. Whenever it is properly applied, therefore, trade activities cannot possibly be controlled in such a manner as to produce an excess of exports, nor ought they to be directed, with a view to causing an excess of imports. The link system is adopted, therefore, as a most effective method of keeping the total trade results in equilibrium.

The next question that attracts our attention concerns the characteristics of this function of balancing international trade results. Traditionally, the trade balance has been sought in respect to the total trade results of a state. The recent tendency under controlled trade conditions is towards balancing trade with all countries as far as possible. As we have discussed elsewhere, the trade equilibration which is supposed to have been effected by the barter system, the quota system and the licence system consists of an equilibration of the trade balance with all other countries. In this respect the link system differs from these other systems, since it is designed to bring about an equilibrium in each trade link. The operating unit of link trade being individuals or organizations, the equilibration of trade results is obtained, in the first place, individually, that is to say by each operating unit. Secondly, a trade equilibrium is obtained by linking each import trade with the appropriate export trade. Thus the manner of equilibrating a foreign trade balance has manifested three successive stages of development. The trade results, which were equilibrated

in the first stage collectively, on the basis of the entire trade of a state, were made in the second stage to balance according to each trading country, and finally individually in each trade link. This evolution in the process of trade equilibration would indicate a corresponding development in the methods of securing a trade equilibrium, namely, through progressive changes from automatic equilibration to controlled equilibration, and finally to legally enforced equilibration.

Thus the link system fulfils the three-fold function of promoting the export trade, moderating import restrictions, and balancing foreign trade results. While the system has been endorsed in this country mainly in connection with the first-mentioned function, a successful discharge of this function depends, as has already been pointed out, more upon various other factors than upon the successful operation of the system itself. As for the second function, its success also depends upon the extent to which the system succeeds in promoting the export trade. It would now seem that the most effective and unique function of the link system consists in the achievement of individual trade balance. However, this system has so far operated only in a partially and within certain limited areas of our foreign trade activities, and therefore it is only after its enforcement has been carried out on a wider scale that the system can be expected to make more effective contributions to our foreign trade in general.

5. VARIOUS TYPES OF THE LINK SYSTEM

1. It has been shown that by linking imports with exports, or exports with imports, the link system can be divided into a system of obligatory export and a system of import privilege. This classification is applicable to each of the types enumerated below. In ordinary link trade, however, import permits are issued on the basis of the export already completed and since this system of import

privilege is the more rational method of conducting link trade, the following types of the link system should be considered to fall under this latter types of link trade.

2. According to the manner of establishing the link between the various classes of merchandise, the system may be divided into a collective merchandise link and an individual merchandise link. The former links a certain volume of exports with a corresponding volume of imports without any definition of the merchandise. The latter links certain specified exports with specified imports, in most cases the export of manufactured goods being linked with the import of their respective raw materials.

3. The system can be divided into an individual link system and a group link system in accordance with the trading unit to which it is to be applied. Under the individual link system, it would be necessary to permit the transfer of import privilege, since few traders undertake both export and import business with an equal turnover. When the trading unit is a joint organization of import associations and export associations, the system is convenient, since both export and import transactions are then conducted jointly under one organized unit.

4. Classified on the quantitative basis of link trade, the system can be divided into a link established in terms of value and one established in terms of quantity of merchandise involved. The former link is established between certain specified or unspecified imports and exports on the basis of their respective total value, regardless of the quantity of merchandise involved. In the latter case, the import of a certain quantity of raw materials is permitted in link with the export of a certain definite quantity of the corresponding manufactured products. In some cases of the latter type of link system, the import of raw materials is permitted in such quantities as are contained technically in the corresponding products exported, while in other cases the link is established in terms of definite quantities regardless of such technical considerations.

5. As regards the ratio at which the link is to be established between exports and imports, the system may be divided again into a link of equal amounts and a link of differential amounts. The former system permits imports in amounts equal to those of the corresponding exports, while the latter involves the permits of smaller amounts for imports than for exports. The difference between the volume of imports and the volume of exports usually varies in accordance with the nature of the import merchandise.

6. According as to whether or not import merchandise is subject to discrimination, the system divides again into an impartial link and a discriminative link. The former system handles all import merchandise on an equal basis, while the latter involves certain discriminations varying with the intensity of the need for the specified import in the national economy. Such discriminations ordinarily consist of differential ratios in trade link.

7. The link system is divisible again into an inclusive link system and a partial link system. The former system is one which places all imports under its control regardless of whether they are destined for export for military use or for popular consumption. The latter places under its control only such imports as are manufactured into exports, and ignores supplies intended for military purposes or for popular consumption, placing the first classification on a preferential basis and prohibiting or restricting the importation of items belonging the second category.

8. On the basis of presence or absence of a due date on import permits or export obligation, the system can be still further classified as link trade with due date and link trade without due date. In case a permit is granted in return for completed export, the permit ordinarily does not bear an expiration date, the importer being allowed to exercise his right at his pleasure. On the other hand, an obligation to export, resulting from licenced import business, usually accompanies a due date.

No critical analysis will be made, in the present

treatise, of the various forms of the link system which have been or will soon be enforced in this country. However, a few remarks may be added regarding the types of the system just discussed. The wool link system, put into effect on March 15, 1938, is an individual merchandise system that establishes a link in terms of volume of merchandise, allowing imports up to the volume of exports. The export obligation arising from the system is due dated, the importer who obtains an import permit being required to export within ten months woolen products representing the volume of raw materials previously imported. Though details are still unpublished as to the cotton link system which is to become effective in the near future, it is reported that the system is to be enforced as an individual link system, with cotton mills as the principal operating units. It is rumoured that it will take the type of an individual merchandise system, allowing imports in terms of quantity of merchandise, with export obligation to be fulfilled within two months, in case the trade is mediated by an exporter. Of the various other systems reported as being under consideration the rayon link system, for example, is said to comprise an individual link system dealing with rayon yarn and a group system dealing with rayon piece-goods. Individual merchandise link systems will soon be enforced, it is reported upon bristles and brushes, beef-tallow and soap, noil and felt hats, rubber and rubber goods, South Sea lumber and veneer boards, leather and leather goods, etc. It is reported also that a number of collective merchandise systems linking various classes of exports with imports will be enforced in the near future. However, detailed discussions on these systems remain beyond the scope of this treatise, our present concern being with the theoretical aspect of the link system.

(July 20, 1938)